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SUBJECT: LITTLE PROGRESS ON RESOLVING BOT AND CARGILL/ADM  
INVESTMENT ISSUES

REF: ANKARA 3343

1. (SBU) Summary: Turkish authorities are making little if any progress toward resolving the investment disputes involving U.S. power generation and starch-based sweetener companies. The BOT issue is being held up in part due to disagreements between the Energy Ministry and the Energy Market Regulatory Authority (EMRA); each is waiting for the other to act, and neither is communicating with the companies. The EMRA President assured us this week that, if the problem remains unresolved when the end-August licensing deadline hits, he will unilaterally extend the deadline to allow the companies to continue to operate. On the sweetener issue, Cargill has made some progress in its legal battles over zoning, but understands that Industry Minister Coskun has tentatively decided not to increase the quota for starch-based sweetener production from 10 to 15 percent, as was done last year. If Coskun sticks to this decision, both Cargill and ADM will face major difficulties. End Summary.

2. (SBU) During the past week, EconCouns met with Energy U/S Sami Demirbilek and Energy Market Regulatory Authority (EMRA) President Yusuf Gunay to express concern about the lack of progress in resolving the issues surrounding U.S.-owned and USG-supported BOT power generation projects. As reported in reftel, the fundamental problem is that the Energy Ministry has been pressing the power generation companies (in a heavy-handed manner) to reduce their prices, or risk not having their new license applications approved by EMRA. (Note: Under EMRA regulations, all power generation companies, including those already operating, are required to apply and obtain new operating licenses. EMRA officials insisted this was a pro forma process for existing companies, but Ministry officials indicated it might not be. Moreover, the language in the license applications suggested the companies might be giving up their existing contractual rights by applying. End note).

3. (SBU) EconCouns reminded both Demirbilek and Gunay that, during a May 2003 visit to Ankara (reftel), a group of international export credit agencies had expressed concern about these developments and had urged the GOT to clarify in writing that the companies, by applying for new licenses, would not give up any of their existing contractual obligations. They also had suggested that any GOT move to violate or force changes in existing contracts would have negative consequences for Turkey's broader efforts to attract investment into the sector. (In response, GOT officials had promised to clarify that the companies would not give up their existing contractual rights by applying for new licenses, and had insisted that they had no intention of violating contracts. Rather, they were only asking the companies to work with them to facilitate Turkey's transition to a market-based energy sector.) Following the meeting, OPIC had sent a letter to the EMRA President highlighting the areas of discussion and the GOT commitments.

4. (SBU) EconCouns noted that, two months later, the GOT has neither issued the promised clarification nor responded to the OPIC letter. With the deadline for issuance of new licenses fast approaching (end-August), we are increasingly concerned about the lack of progress. EconCouns asked how GOT authorities plan to resolve this problem.

5. (SBU) Demirbilek said there were many possible solutions to the problem, but under any circumstances the GOT would not

violate or unilaterally abrogate the contracts. The first step, however, is for EMRA to forward its proposals on how the contracts could be revised to facilitate Turkey's shift to a market-based electricity system. The Ministry would review those proposals, and then try to find a solution. Despite repeated queries, Demirbilek did not comment on why the GOT had failed to provide the promised clarification of the companies' rights under the existing contracts. In a troubling aside, he noted that the Ministry had determined that one of the companies -- Doga (partly owned by U.S.-based Edison Mission) -- was violating the terms of its contract, and was continuing to look into the other companies' performances. (Note: A standard GOT approach on domestic and international energy issues has been to use a minor, technical violation of contracts to force concessions from its "partners.")

16. (SBU) Gunay countered that EMRA was in no position to present proposals to the Ministry, and in any case the Ministry had no right to judge the utility of any proposals. Instead, Gunay has asked the companies to offer ideas on how they could facilitate the sector's transition. These might include, for example, giving up government purchase guarantees in return for a longer operating period before they turn the projects over to the government. Unfortunately, Gunay said, the Ministry's approach on prices has "turned off" the companies, making them defensive and unenthusiastic about offering any concessions. Gunay said price should not be the issue. Sure, the contract prices are high, but the GOT signed these contracts and thus has no grounds for complaint.

17. (SBU) As for next steps, Gunay said he had written to the Ministry advising that EMRA had reached the licensing stage. He is not seeking the Ministry's approval, but wants to be able to show that the Ministry was aware that EMRA would be issuing licenses so that they could not later blame EMRA for issuing licenses and thus undermining the Ministry's efforts to obtain price concessions. If the Ministry responds to his letter by saying it is about to reach agreement with the companies on a new price, he will extend the licensing deadline to allow the agreement to be concluded. If the Ministry says there is no such agreement, he will issue the licenses. He urged us not to worry, saying that, in the worst case, he would extend the licensing deadline so the companies could continue to operate. Gunay added that he would respond to OPIC's letter as soon as he heard back from the Ministry.

18. (SBU) In a separate meeting, Cargill executives updated us on the problems facing both the company and the broader starch-based sweetener industry, including U.S.-based ADM. There has been some progress on the Cargill-specific issue, which involves legal actions against its factory for being improperly zoned. The Danistay (State Council) had recently rejected two law suits aimed at annulling its construction license, based on the Danistay's view that the plaintiffs had no legal basis for suing. However, the Danistay had ruled against Cargill in a third case -- brought by the same plaintiffs -- involving the plant's emissions permit, based on the argument that, since the plant was improperly zoned, its emissions permit was improperly issued. Cargill is appealing this decision, and generally sees the Danistay's actions as positive. Meanwhile, senior Industry Ministry officials, including Minister Ali Coskun, continue to tell Cargill that they expect to submit to Parliament a new industrial zoning law, which would effectively enable Cargill to "re-zone" its factory, in September. (Note: Cargill executives are a bit skeptical, as Coskun has been promising action on this for some time.)

19. (SBU) The other issue, which affects ADM as well as Cargill, is how the government will implement the sugar production quota. Under the Sugar Law, the Sugar Board sets an annual production quota for the entire sweetener industry (sugar, fructose, glucose), and fructose/glucose producers such as Cargill and ADM are limited to 10 percent of the quota. Last year, the government set the total quota significantly above domestic demand (2,340,000 tons compared to domestic demand of about 1,850,000 tons), and raised the fructose/glucose sub-quota to 15 percent (as allowed by the law). These two moves enabled starch-based sweetener producers to continue operating at reasonable levels, even if below capacity.

110. (SBU) This year, however, Cargill has heard that Minister Coskun is siding with the sugar beet producers and is planning to keep the sub-quota at 10 percent (though the overall sweetener production quota will remain at 2,340,000 tons). If he sticks to this decision, the starch-based sweetener producers will be forced to produce at far below

capacity, raising serious questions about their ability to continue. Cargill and ADM have organized a group made up of their major customers -- the cola, fruit juice, and confectionary companies -- to meet with Prime Minister Erdogan in the coming weeks to lobby for a 15 percent quota. If this approach fails, Cargill and ADM might ask the Embassy to weigh in (until now, they have kept us informed but asked us not to weigh in).

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